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In the Supreme Court of the United States

OCTOBER TERM, 1983

OCEAN SANDS HOLDING CORPORATION, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR
THE FOURTH CIRCUIT*

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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Petitioners contend that the court of appeals erred in several respects in affirming a Tax Court decision finding them liable for taxes on unreported income, and, in the case of two of the petitioners, for additions to tax as a result of fraudulent underreporting of income.

1. Petitioners are either members of the R. Wilson Chaplain family or corporations owned by that family (Pet. App. A24, A33-A35). Two of the corporate petitioners, Ocean Sands and Colony, owned oceanfront motels in Virginia Beach, Virginia. A third, Sea Fin, owned a smaller motel and a trailer park. The other two corporate petitioners owned parking lots (*id.* at A32-A35). The Chaplain family refused to recognize the separate existence of their corporations, treating them collectively as a single enterprise (*id.* at A37-A38). The Chaplains also failed to keep

adequate business records, and they alleged that whatever records they did maintain had been either stolen or destroyed in one of three separate fires (*id.* at A38-A43).

Respondent reconstructed petitioners' income for various years between 1965 and 1974 by a variety of methods, including estimates based upon the incomes of comparable neighboring motels (Pet. App. A47-A55, A70-A74). Respondent then asserted income tax deficiencies based upon these estimates. Respondent also asserted a 50% addition to the taxes of some of the individual petitioners and to the taxes of Ocean Sands, Colony, and Sea Fin, based on the fraudulent underreporting of income for the years involved (*id.* at A12-A15).

The Tax Court consolidated the several related cases of the various petitioners. It generally accepted respondent's determinations, but it reduced the asserted reconstructed motel income figures by 15 to 25% (Pet. App. A64-A65). The Tax Court declined to impose a fraud penalty upon the individuals or upon Sea Fin, but it upheld the fraud penalty against the other corporate petitioners (*id.* at A132, A139-A141, A159-A160). The Fourth Circuit affirmed (*id.* at A197-A204).

2. Petitioners contend (Pet. 22-24) that the reconstructed income figures advanced by respondent, and later reduced by the Tax Court, were deliberately overstated so as to deny petitioners the opportunity to pay the taxes asserted and sue for a refund in district court, thus denying petitioners their constitutional right to a jury trial. This contention is without merit. It is well established that a taxpayer's inability to pay an asserted deficiency does not entitle that taxpayer to bring a refund suit, especially where, as here, the taxpayer may obtain a preassessment judicial review of its tax liabilities in the United States Tax Court. See *Flora v. United States*, 362 U.S. 145 (1960). Here, the fact that respondent's

original estimates of unreported income may have been too high is partly attributable to petitioners themselves, because they consistently refused to cooperate with respondent's investigation of their tax liabilities for the years in question (see Pet. App. A48-A49). Moreover, the record in this case fails to show that the assessments were deliberately overstated or, indeed, that petitioners lacked the resources necessary to pay them and sue for a refund in district court.

3. Three corporate petitioners assert (Pet. 27-39) that the Tax Court's reduction of the asserted deficiencies removed the presumption of correctness that ordinarily attaches to respondent's determination of deficiencies. See *Welch v. Helvering*, 290 U.S. 111, 115 (1933). However, this argument ignores the fact that respondent did *not* rely upon any presumption of correctness here. To the contrary, respondent in these cases bore the burden of establishing fraudulent understatements of income, under Section 6653(b) of the Internal Revenue Code of 1954 (26 U.S.C.). Accordingly, from the outset respondent undertook the task of going forward with the evidence. The Tax Court evaluated this evidence, and, having made substantial downward adjustments to the deficiencies in light of petitioners' presentation, made its findings. In view of respondent's evidentiary presentation, there is no question here of the validity of a "presumption of correctness."¹

¹Petitioners' attack (Pet. 43-49) upon the application of the six-year statute of limitations to Ocean Sands also misses its mark. Section 6501(e) of the Internal Revenue Code of 1954 (26 U.S.C. (& Supp. V)) provides for an expanded six-year statute of limitations with respect to assessments against taxpayers who understate gross income by more than 25%. Here, the Tax Court found (Pet. App. A189-A190) that Ocean Sands' reported \$29,106 income for 1967 — when compared to the Tax Court's redetermined figure of \$62,010 — was understated by more than 100%. This understatement made the deficiency determination of March 10, 1972, timely without regard to the fact that respondent had assessed an even greater deficiency. Petitioners attack the

4. Petitioners also contend (Pet. 39-43) that the Tax Court erred in failing to accept at face value the estimates of depreciation made by the Chaplains with respect to petitioners' motels. These estimates were based upon the Chaplains' hasty and self-serving reconstructions from memory of the building costs of the motels (Pet. App. A87-A88). The Tax Court lowered the Chaplains' appraisal by taking into account property tax valuations, amounts of financing provided for the properties, and other objective factors (*id.* at A89-A90). In refusing to accept the Chaplains' self-serving testimony as controlling, the Tax Court acted well within its authority as the trier of fact. See, e.g., *Potts, Davis & Co. v. Commissioner*, 431 F.2d 1222, 1225 (9th Cir. 1970).

5. Petitioners Ocean Sands and Colony contend (Pet. 49-62) that they should not be liable for penalties attributable to fraudulent underreporting of income, because the Tax Court refused to impose such penalties upon the other corporations or upon the Chaplains individually. Once the Tax Court has made a finding of fraud, however, that finding is not subject to reversal unless shown to be "clearly erroneous." See, e.g., *Marsellus v. Commissioner*, 544 F.2d 883, 885 (5th Cir. 1977). The Tax Court's finding of fraud here on the part of only *some* of the petitioners is not, *ipso facto*, "clearly erroneous." To the contrary, this finding reflects the careful appraisal made by the Tax Court of the evidence before it. That evidence more than sufficed to show fraud on the part of Ocean Sands and Colony.

computation of the \$62,010 figure, asserting that the Tax Court erroneously relied upon an uncertain "linen use" method that was rendered inaccurate by the delay (see Pet. 45-47). However, petitioners' argument ignores the fact that the Tax Court rejected the linen use method and instead relied upon figures for comparable motels (see Pet. App. A63).

Even after it had discounted respondent's reconstructed income figures, the Tax Court still properly found fraud based upon the evidence of petitioners' consistent and substantial understatement of income, refusal to cooperate with investigative authorities, failure to keep adequate records, suspicious destruction of those records that did exist, obfuscations of intercorporate dealings, and transactions involving large amounts of cash (Pet. App. A132-A139). The court's determination plainly is supported by substantial evidence, and petitioners' attempt (Pet. 54-62) to ask this Court to reweigh that evidence is inappropriate. See *Helvering v. Kehoe*, 309 U.S. 277 (1940). As the Ninth Circuit stated in *Bahoric v. Commissioner*, 363 F.2d 151, 154 (1966):

The attack of petitioners' counsel * * * is made by compartmentalizing the elements and going to work on each singly. But, in the end, they must all be brought together. Treating the facts as a bundle, [there is] nothing clearly erroneous about the tax court's decision.

In this case, the court of appeals has affirmed in all respects the Tax Court's painstaking and thorough decision in these factually complex cases. Petitioners have failed to show error in this decision,² and they have failed to indicate any conflict in decisions or administrative importance of the issues presented. Accordingly, further review is unwarranted.

²The court of appeals correctly rejected petitioners' argument (Pet. 24-27) that the Tax Court abused its discretion in consolidating the cases. As the court explained (Pet. App. A202-A203), consolidation was appropriate in light of the common issues presented as a result of the Chaplains' treatment of their separate corporations as parts of a single family enterprise.

**It is therefore respectfully submitted that the petition for
a writ of certiorari should be denied.**

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